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AUTHOR	Augenblick, John
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ABSTRACT

The history of school finance reform in the last 75 years provides a context for considering future school finance issues and the different school finance problems faced by the various states. From 1900 to 1965 states provided foundation aid to school districts. In the mid-1960s federal aid was added for special needs students. In the late 1960s and through the 1970s, court litigation became the locus of school finance reform efforts, focusing on equal protection arguments and variations in district needs. Tax reform also became an issue. Now, most states are more sensitive to property wealth-related inequities in educational finance. Future issues in school finance will involve district size, municipal overburden, alternative sources of district revenues, educational adequacy, public support for private education, and teacher salary levels. States can be grouped according to six school finance problems they wil face in the 1980s, including those with pending school finance or municipal overburden cases, those anticipating reforms or reviewing past reforms, those facing fiscal crises, and those where reforms are likely in the next few years. (RW)

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WORKING PAPERS IN EDUCATION FINANCE

Working Paper No. 38

SCHOOL FINANCE: PAST, PRESENT AND FUTURE ISSUES IN THE STATES

by John Augenblick

Education Finance Center
Education Programs Division
1860 Lincoln Street, Suite 300
Denver, Colorado 80295
(303) 830-3646

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THE CONTEXT OF SCHOOL FINANCE REFORM

In order to place the future direction of states in school finance reform in context, it is appropriate to review the historical development of the issue. Where we are, and where we are going depends both on where we have been and the special circumstances that will characterize the future.

School finance reform is not a new issue. The primary concern -- that the amount of money spent per child is largely determined by the property wealth of the school district, termed wealth related inequity -- has been recognized for 75 years. At the turn of the twentieth century, the major mechanism for state aid to education was the flat grant approach in which funds were distributed on the basis of equal dollars per child to each school district. The flat grant approach violated at least two basic principles that need to be considered in any intergovernmental aid structure. First, aid should be distributed on the basis of the need of the receiving jurisdiction. If education is being supported, some assessment of the education task facing the service provider should be undertaken. Second, if the receiving jurisdiction is providing its own support, an assessment of the ability of that jurisdiction, or at least its capacity relative to other similar jurisdictions, should be undertaken. Essentially, improvements in state aid systems developed between 1900 and 1965 were designed to make the allocation of aid more sensitive to the wide variations in the property wealth of school districts. The most popular approach, the foundation program, made the state a

partner with local school districts in guaranteeing that a specific minimum amount of funds would be available at a uniform tax rate.

By the mid-1960s, numerous events led to a renewed interest in school finance. Questions were being raised about the equity of school systems a decade after the desegregation activities that followed the 1954 Brown decision in which the U.S. Supreme Court declared desegregation in the public schools to be unconstitutional. Concern about the quality of education services remained high, derived in part from post-Sputnik (1957) interest in improving technological education and in part from increasing public interest in accountability. Finally, the initiation in 1965 of major federal involvement in education, through the enactment of the federal Elementary and Secondary Education Act (ESEA), focused attention on the specific needs of special populations of students, particularly those in need of special education services.

By 1968 it was recognized that school finance systems designed to overcome wealth related inequities did not necessarily accomplish the additional objective of providing aid to districts based on the education needs of students. Up to some point, state aid guaranteed a similar level of expenditures for all students while beyond that point, what was provided was a function of local property wealth, local willingness to tax or both. No mechanism assumed that districts with different education needs would receive the resources required to deal with them.

This shortcoming led to the initiation of litigation designed to declare illegal those state aid systems that were not sensitive to the varying education needs of students. It did not take long, however, for the courts to respond that the issue was not justiciable. In McInnis v. Ogilvie, the plaintiffs, children from a property-poor Illinois school district, requested, as a remedy for the inequity they alleged, that public school revenues be allocated in proportion to student "needs." The court essentially ruled that not only was it difficult to identify the education needs of students, but it was impossible to translate such needs into fiscal terms that could be incorporated into a process for distributing aid.

The failure of the legal approach, combined with the recognition that legal action was needed in order to spur legislative change, led to the creation of a new legal strategy. This new approach was based on an equal protection argument and the successful outcome of its use in the 1971 Serrano decision, in which the California Supreme Court overturned California's education funding system, led to renewed interest in education finance. Unfortunately, the equity standard that evolved was a negative one, fiscal neutrality, which stated that the quality of public education may not be a function of the wealth of a pupil's parents and neighbors. This elusive concept tended to focus attention on interdistrict taxpayer concerns and not on education needs. The strengths of this approach were muted by the failure of the U.S. Supreme Court to uphold the Rodriguez decision in 1973

-- a decision that found Texas' education finance system to be unconstitutional.

Following quickly on the heels of the Rodriguez decision were numerous cases focusing on state education clauses that required the provision of "thorough," "efficient," "ample" or "basic" education. In order to define these concepts it became necessary to deal not only with wealth related inequities but education needs. These cases stimulated an interest in being able to accomplish precisely what had not and could not be addressed less than a decade earlier: the determination of the education needs of pupils and the levels of resources required to deal with such needs. In combination with expanded federal and state programs for the handicapped, the bilingual and other types of students, these cases sought to link the wealth related and need related inequities. Further, some of these cases also identified characteristics of districts as requiring special attention by state aid systems. By the end of the 1970s it had become necessary to create state aid programs that were sensitive to pupil related and district related resource need variations in conjunction with the wealth related issue.

The greatest problem faced by state aid systems today is to determine the legitimate variations among school districts, those caused by factors over which districts have little or no control: size, cost of providing services, proportions of students with different special needs and so on. It is no longer sufficient to assume that equity is achieved when the per pupil expenditures of districts are equal; rather, it is of critical importance to

permit variations among districts when they are caused by legitimate factors.

Another major thrust for school finance reform in the 1970s, in addition to the litigation, was tax reform. This concern has been expressed in many ways and it has changed over the last decade. In the beginning of the 1970s, the primary tax related issue was property tax reform. This topic included improvement in assessment practices as well as an interest in a reduction of property tax levels. One response to this issue was the creation of circuit breaker mechanisms designed to reduce the burden of property taxation on low income families. There was also a concern about the ability of tax systems to generate necessary revenues. Given the high rate of inflation that has characterized the last decade, it appeared that state revenue systems would not be capable of providing necessary funding for newly-demanded social services and accepted services that faced higher costs. By the end of the 1970s, concern had shifted to the general burden of all taxation, and to some extent the equity of that burden. The interest in tax or spending limitations reflected an interest in reducing all taxation.

Analyses of school finance reform suggest that the concerns for changes in the tax system were addressed to a greater extent than concerns about equalizing the expenditure levels of school districts. School finance reform was characterized by: (1) a decreased reliance on local revenues with a concomitant increase in state revenues and thus a shift from property taxation to income and sales taxes; (2) improvement in the equity of tax

systems because of the shift away from property taxes, improvements in the property tax system and a reduction in the variation of funds generated by districts per unit of tax effort; (3) a reduction in the relationship between district property wealth per pupil and expenditures per pupil; and (4) an increase in the relationship between district tax rates and expenditures per pupil, indicating that tax effort, rather than wealth, was a determinant of interdistrict per pupil spending variations.

After 15 years of effort, a great deal has been accomplished by school finance reform. While there is much to be proud of, a great deal of work remains. Most state aid systems are now more sensitive to the wealth related inequities that have been identified for so long. This has been accomplished through the creation of high level foundation programs or forms of district power equalizing systems. Most recently, states have combined these approaches into two-tiered systems that guarantee minimum expenditures per pupil for all districts and give them an equal opportunity to raise funds beyond that level. Some states have made their aid systems more sensitive to pupil related or district related needs, through categorical programs or through pupil weighted approaches. While these approaches are not free of problems, they are being improved in order to provide funds in an equitable and efficient way. Finally, some states have created mechanisms to promote greater pupil equity or to limit local taxation through the use of budget caps, expenditure increase limitations or budget review procedures. This activity has interferred with traditional notions of local control. While

local control remains a symbol of the education system, it is also the greatest impediment to achieving equity. Balancing equity and local control in an era of fiscal constraints and a changing demography will be as significant a challenge to promoters of reform as separating legitimate from illegitimate variations in spending among school districts.

FUTURE ISSUES IN SCHOOL FINANCE

Since 1968, nearly 30 states have reviewed their school finance systems and modified them in fundamental ways. In general, greater strides were made in reducing tax related inequities than in alleviating variations in per pupil expenditure levels across school districts. Numerous problems now face the states as they attempt to deal with court mandates, adapt to changes in the federal role, modify their revenue generation systems and continue to limit education spending while promoting an adequate and equitable education system.

The states will continue to increase the sensitivity of their school aid systems to school districts with special characteristics. Important among the factors that will be considered are size and municipal overburden. It is generally recognized that small school districts incur higher than average per pupil costs. In the past much effort has been expended to consolidate small districts to make them more efficient. The conventional wisdom concerning consolidation has generally been abandoned, however, due to offsetting increases in transportation

costs and to an interest in preserving local social institutions. States that have numerous small districts, such as Oklahoma, Nebraska or Texas, must now determine how much additional support small districts need to receive in order to operate adequate school programs. It is also felt, and the courts may require, that urban school districts should receive additional state support. Not that long ago, city schools typically offered outstanding education programs. As the fiscal condition of many cities changed, with decreasing tax bases and increasing public service demands, support for education has deteriorated. In order to assure the adequacy of education programs, additional state education support may need to be allocated to cities.

Another issue that has begun to receive attention in the states is alternative sources of local school district revenue. Most school districts rely almost completely on the property tax base as the source of local support. Fiscally dependent school districts often derive revenues from sales and other taxes imposed by the jurisdictions of which they are a part. In Iowa, school districts have the authority to impose an income tax, although few take advantage of the opportunity. In other states, such as Pennsylvania, a head tax can be imposed. In a few states, a portion of the income tax revenues collected by the state are returned to the school districts, although such revenue may then be deducted from state aid. Many districts have considered the imposition of fees for particular services. The reorganization of the intergovernmental fiscal structure of the country is not likely to result in a definitive relationship between functions to

be performed by governments and sources of revenue that they, and they alone, can use. Given the unpopularity of the property tax and the continued decline in reliance upon it, it is crucial that local school districts have access to other tax bases if they are to provide a significant share of education support.

A problem that is likely to be exacerbated in the 1980s is the variation among states in the adequacy of their education systems. In the 1970s there was some discussion of a federal role in helping to equalize educational programs around the country for all pupils, not just those with special needs. Given the changing federal role, this is an unlikely possibility in the future. What is becoming clear, however, is that some states are facing extreme economic difficulty, including Massachusetts, Michigan and Oregon, and some states are facing economic prosperity, including Wyoming, Colorado, Texas, Oklahoma and North Dakota. It is likely that these differences will translate into relatively weak or relatively strong support for education. While education is a function of the states, the growing differences in the adequacy of educational programs, reversing an opposite trend over the last two decades, may spark interest in using federal aid as a remedy.

A major policy concern in the next few years will be public support for privately sponsored education. Tax credit legislation was strongly supported at the federal level, although implementation may depend on the achievement of a balanced budget. Tax credits will be on the ballot in Washington, D.C. and vouchers continue to receive support in California. The resolution of this issue will have an important long-term impact on the governance

and financing of public education. This is another area in which the issues of quality and local control will be balanced against equity.

Finally, an important education finance issue looming on the horizon is teacher salary levels. During the past decade, gains have been made in raising teachers' salaries although such gains did not go far beyond the impact of inflation. At the same time, new job opportunities have opened for those who traditionally chose teaching as a profession. The teaching profession may not be capable of attracting well-trained individuals unless the incentives offered are modified in fundamental ways. This is a complex issue because while it may not be necessary to offer windfall bonuses to currently practicing educators, it may be necessary to offer high salaries to new professionals or to the very best practitioners. Any approach that undertakes this differentiation flies in the face of current practice; approaches that do not differentiate may be extremely costly.

The resolution of the salary issue may be the single most important one of the next 10 years. Given the political power attributed to teacher organizations, this issue will keep education finance in the forefront of state fiscal concerns. Resolving the salary problem in conjunction with balancing quality, equity and local control is likely to demand the continued attention of state policymakers well into the 1980s.

THE AGENDAS FOR SCHOOL FINANCE IN THE STATES

While it is difficult to predict what the states will be doing with regard to school finance reform in the 1980s, it is possible, based on current information, to group states that are facing particular problems. The following groups reflect information available to the Education Finance Center from numerous sources. Some states should appear in more than one group.

Group 1: States with Major General School Finance Cases Pending

In Arkansas, Colorado, Georgia, Maryland and New York cases typical of those of the 1970s have been heard at various levels of the court system. Decisions are expected in these cases within the next six months. This activity would indicate continued interest in school finance, in the persistence of problems identified during the last decade and in the use of litigation as a way of encouraging state legislatures to consider the issues.

Group 2: States with Court Cases Focusing on Municipal Overburden

There is current litigation in Wisconsin that focuses on one of the district related causes of variations in resource needs, municipal overburden. The Maryland and New York cases also contain this issue as a major element. A similar concern is expected to be raised in Connecticut soon. Municipal overburden has several aspects, some of which can be dealt with more easily than others. The fact that cities have higher proportions of

pupils in need of special services or that cities face higher costs in providing educational services can be addressed. The fact that cities face other noneducation-related problems and that these should be addressed through the school aid system is more difficult to analyze or resolve.

Group 3: States in Which Reform is Anticipated

During the last year, studies of school finance have been undertaken in Delaware, Mississippi, Oklahoma and Wyoming. These studies have addressed numerous complex problems faced by those states. While such studies do not, of themselves, indicate that the state aid system will change, they are encouraging in that, in all cases, legislative participation was included.

Group 4: States Reviewing Past Reform Efforts

School finance reform tends to be an ongoing activity and not something that, once done, need never be reviewed. Several states that have modified their state aid systems are now in the midst of reviews or about to initiate a review, including Illinois, Kansas, Missouri, New Jersey, South Carolina, South Dakota and Washington. The reasons for the need to review vary from state to state. In Illinois, there is interest in a general, broad review prompted in part by the need for tax reform. In Kansas, the use of the income factor in the measurement of a district's ability to raise funds is being scrutinized. In Missouri, the use of cost-of-education indices, which seek to balance differences among districts in the cost of providing educational services of similar quality, and new revenue mechanisms could modify the 1977 reform effort. New

ersey's system has been closely watched for several years and a new court case has emerged. South Carolina is reviewing its pupil weighted system. South Dakota passed a reform bill three years ago but chose not to implement it until 1982 after comparing it with its current aid system. Necessary revisions are now being prepared. Washington passed a comprehensive school finance law several years ago but several aspects of that law remain problematic, including teacher salary levels.

Group 5: States Facing Major Fiscal Problems

School finance reform is not immune from the general fiscal pressures facing states and this year, in several states, such pressures are severe. In some cases those pressures have arisen because of voter initiated tax or spending limitations, such as in California, Idaho or Massachusetts. In other cases, the fiscal pressures are caused by poor performance of state revenue systems, as in Michigan, Ohio and Oregon. In most cases, these states face the problem of trying to maintain reform efforts initiated prior to the emergence of fiscal constraints. This is likely to be a politically volatile subject.

Group 6: States Where Reform is Likely to Take Place in the Next Few Years

A number of states appear ready to reform their school finance systems. The impression of "readiness" is not based on scientific study but rather on isolated actions that would need to be more formally structured to assure change. North Dakota is unique this year in having a major increase in state support for

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Education Commission of the States
1860 Lincoln Street, Suite 300
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